No. 22217

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

HOLLYWOOD NATIONAL BANK,

Appellant,

vs.

A. J. BUMB,

Appellee.

APPELLANT'S REPLY BRIEF.

MANATT & PHELPS,

6842 Van Nuys Boulevard,
Van Nuys, Calif. 91405,

Attorneys for Appellant,
Hollywood National Bank.

Parker & Son, Inc., Law Printers, Los Angeles. Phone MA. 6-9171.

TOPICAL INDEX

TABLE OF AUTHORITIES CITED

Cases — Page

Statute

Textbook

No. 22217

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

HOLLYWOOD NATIONAL BANK,

Appellant,

vs.

A. J. BUMB,

Appellee.

APPELLANT'S REPLY BRIEF.

Question Presented.

It is not sufficient to state the issue presented by this case merely in terms of whether the bankruptcy court has summary jurisdiction over the parties (as appellee's brief does, expressly on page 2 and impliedly throughout the brief). The question is, summary jurisdiction for what purpose? *i.e.,* summary jurisdiction over what controversies between the trustee and appellant? It is true that, as escrow holder, appellant was an agent of the selling trustee and of the buyer to carry out their instructions, and bore a fiduciary relationship to each of them. The issue is whether the trustee can invoke the summary jurisdiction of the bankruptcy court to get a money judgment for damages allegedly resulting from a breach of the escrow instructions by the escrow holder.

The question is whether such a suit is strictly or properly part of the proceedings in bankruptcy.

Moreover, the issue is presented in its starkest form inasmuch as the trustee initiated summary proceedings for damages for $81,610.22 without attempting to recover the real property conveyed to the buyers. The buyers (Fleming Brokerage Company and San Ysidro Ranch Corporation) still owned the property at the time the summary proceedings were initiated, and they are parties from which the trustee is seeking damages; nevertheless, the application [R. 1-43] and the order to show cause [R. 44-45] are silent as to recovery of the property.

The Basic Fallacy of Appellee's Argument.

It is respectfully submitted that there is a tremendous difference between "jurisdiction over property" and jurisdiction over a controversy concerning whether damages resulted from the close of an escrow involving property. If a trustee attempts to recover property or the value of property once in his possession, there is a controversy "over property". However, in the present case, the trustee has chosen not to challenge the right of the buyers to keep the property; instead, the trustee is looking to appellant, as the escrow holder which allegedly closed the escrow improperly, to pay $81,610.22 in damages. The *in rem* jurisdiction of the bankruptcy court simply is not appropriate for the trustee's controversies with appellant, controversies as to whether appellant breached its contract as stated in the escrow instructions and as to whether damages resulted even if there was a breach.

These controversies are not "controversies over property" as that phrase is used in the quotation from Section 23.05 of *Collier* on page 5 of appellee's brief. What does *Collier* mean by "controversies over property"? Section 23.05 quotes (at pp. 478-479) from *Shea v. Lewis* (8th Cir. 1913), 206 Fed. 877, as follows:

> "The bankruptcy court has jurisdiction to draw to itself, and to determine by summary proceedings after reasonable notice to claimants, the merits of *controversies* between the trustee and such claimants *over liens upon and title to property claimed by the trustee* as that of the bankrupt which has been lawfully reduced to the actual possession of the trustee or of some other officer of the bankruptcy court as the property of the bankrupt. When those in possession are not adverse claimants, but are only representatives of the bankrupt without claim of lien upon, or right to, the property in themselves, the bankruptcy court may by summary proceeding take the actual possession of the property and then, when it has thus acquired the actual possession, may by summary proceedings determine *the validity of claims or liens upon and titles to it.*" (Emphasis added.)

In the present case appellant and appellee agree that the bankruptcy court has summary jurisdiction over the real property, it having been in the actual possession of trustee; but the fact remains that the trustee does not invoke the referee's jurisdiction over the property by raising any issue involving "possession of the property" or "the validity of claims or liens upon and title to it" (*ibid.*).

In *McEldowney v. Card* (E.D. Tenn. 1911), 193 Fed. 475, writ of error dis., 213 Fed. 1020, the trustee in bankruptcy chose to sue defendant "in trover to recover the value of property that had belonged to the bankrupt estate and had been converted by the defendant to his own use after title to the property had been vested in the trustee by virtue of the adjudication in bankruptcy." The court had to decide if the suit was "a controversy with an adverse claimant of the bankrupt's property", and ruled that it was not such a controversy because "the present suit involves no controversy as to the right or title of the trustee to the logs which passed to him as part of the bankrupt estate." (*Id.* at 481.)

Discussion of Cases Cited in Appellee's Brief.

For convenience, the cases cited in appellee's brief are discussed here in the same chronological order in which they appear in appellee's brief. Since appellant does not think that the present case involves the use of the bankruptcy court's jurisdiction over property, the cases cited in appellant's opening brief were not chosen on the basis of who had possession of the property at the commencement of the bankruptcy proceedings. For example, contrary to appellee's statement (p. 5 of his brief) that "i[n] every instance" these cases concern property in the hands of third parties at the commencement of the bankruptcy proceedings, *In re Spur Fuel Oil Sales Corp.* (E.D. N.Y. 1962), 204 F. Supp. 696, is a case in which the court held that the debtor's agent, the assignee for the benefit of creditors, was in constructive possession of the property at the time of the filing of the bankruptcy petition.

In re Spur Fuel Oil Sales Corp., supra, was cited in appellant's opening brief (pp. 8 and 14) in support of the general proposition that the bankruptcy court's summary jurisdiction is confined to matters *in rem.* As a matter of fact, contrary to the statement on page 6 of appellee's brief, the *Spur Fuel Oil* court held that the bankruptcy court did have summary jurisdiction in that case because of the constructive possession of the debtor's agent.

Appellant's opening brief does not state or imply that *Suhl v. Bumb* (9th Cir. 1965), 348 F. 2d 869, cert. denied, 382 U.S. 938, 86 S. Ct. 388, 15 L. Ed. 2d 349, presented the same precise issue as that of the present case. Rather, appellant suggested that certain language of the *Suhl* opinion (quoted on page 15 of appellant's opening brief) was appropriate in a consideration of the present case; appellant stands by that suggestion. It is "particularly true" that the courts "must carefully examine whether the expedited summary process is appropriate" in a situation "where the property in question is a money claim against third parties rather than a physical asset alleged to be part of the bankrupt's estate." (*Id.* at 872.)

Ignoring the reason why appellant cited the case, page 7 of appellee's brief states that *Burton Coal Co. v. Franklin Coal Co.* (8th Cir. 1933), 67 F. 2d 796, "does not represent a situation where the trustee is attempting to recover property from a third party." This is true; it is likewise true that the present case does not represent such a situation. Moreover, if the trustee should attempt to recover the property, such an attempt would not involve appellant, who does not and never has owned or possessed the property.

The case of *In re Houston Seed Co.* (N.D. Ala. 1954), 122 F. Supp. 340, correctly states the limiting effect of Section 23 of the Bankruptcy Act; and this is the reason that the case was cited on pages 10 and 11 of appellant's opening brief. The consideration of when a claim constitutes consent is irrelevant in the present case, but it is very relevant that a party's consent must be given before the bankruptcy court can adjudicate a controversy not strictly part of the bankruptcy proceedings. Actually, the Ninth Circuit case cited by appellee (*Peters v. Lines* [9th Cir. 1960]. 275 F. 2d 919), does not reject the holding of the *Houston Seed* case regarding a claim's effect on consent; the *Peters* court specifically limited its holding to a trustee's petition for affirmative relief arising out of the same transaction as the proof of claim. (*Id.* at 925-926.) The Court pointed out that this is "quite a different matter from holding that submission of a claim is a consent to summary jurisdiction on a counterclaim arising from an entirely separate transaction." (*Id.* at 925.)

The discussion of *In re Eakin* (2nd Cir. 1946), 154 F. 2d 717, on pages 7 and 8 of appellee's brief misses the point. As the discussion recognizes, at the time of filing of the petition the funds were in the possession of the bankrupt's bank, and were thereafter withdrawn by the bankrupt. The bank's defenses (that the funds were trust funds and, alternatively, that the bank had a right to offset) did not affect the question of possession, and the mere existence of these issues could not defeat the summary jurisdiction of the court. If the contents of a safe deposit box had been involved, disputes over the ultimate ownership of the property would not have changed the fact that the property was in the bankrupt's possession.

The significant factor in the *Eakin* case—and in the present case—is that the trustee's action against the bank was not to recover possession of property, but was "an action to enforce a debt . . . where the debtor denies the existence of the debt" (*Id.* at 719). The Court said that such an action "is not within the summary jurisdiction," and "[t]he Trustee, in such a case, cannot claim possession, because the existence of the chose in action is the issue in dispute." (*Ibid.*)

Although the facts are considerably different, the same basic distinction between the recovery of property and the enforcement of a money claim is involved in *Morrison v. Bay Parkway National Bank* (2nd Cir. 1932), 60 F. 2d 41, pet. cert. dis., 296 U.S. 669, 57 S. Ct. 756, 89 L. Ed. 2008. After the trustee had recovered a money judgment against Bay Parkway National Bank (based on the setting aside of a preference), Lafayette Bank purchased all of the assets of Bay Parkway National Bank. The trustee then petitioned for a summary order directing Lafayette Bank to pay the judgment. Although the trustee argued that Lafayette Bank had assumed the obligation owed directly to the trustee, the Court applied the general rule that "a trustee cannot enforce claims for a breach of contract in a summary proceeding, but must resort to a plenary suit." (*Id.* at 42.) (Appellee's assertion that the action against the transferee bank was *plenary* (p. 8 of appellee's brief), is simply not understandable in light of the reported opinion; the first paragraph reads, "The question before us is whether the judgment to recover an unlawful preference which the trustee in bankruptcy obtained against the Bay Parkway National Bank can be enforced in a *summary* proceed-

ing against Lafayette Bank, the transferee of the former bank's assets." *Ibid.;* emphasis added.)

It is submitted that the cases of *Lowenstein v. Reikes* (2nd Cir. 1931), 54 F. 2d 481, cert. denied, 285 U.S. 539, 52 S. Ct. 311, 76 L. Ed. 932, and *Bardes v. First National Bank of Hawarden,* 178 U.S. 524, 20 S. Ct. 1000, 44 L. Ed. 1175, support the propositions for which they were cited in appellant's opening brief (pp. 8, 9-10).

Appellee's quotation (p. 10 of his brief) from *In re Retail Stores Delivery Corporation* (S.D.N.Y. 1933), 5 F. Supp. 892, supports the use of summary jurisdiction for "return of the property", and nothing more. Likewise, the case of *White v. Schlorb,* 178 U.S. 542, 20 S. Ct. 1007, 44 L. Ed. 1183, is limited to the question of the power of the bankruptcy court to compel restoration of property once in its custody. The Supreme Court indicated that its ruling was "not going beyond what the decision of the case before us requires," and that "the questions certified concern, not the trial of the title to these goods, but only the judicial custody and lawful possession of them." (*Id.* at 178 U.S. 547-548, 546.)

The case of *Burnham v. Todd* (5th Cir. 1943), 139 F. 2d 338, deserves special attention here inasmuch as appellee submits that it is "the leading case in this area" and "at least in theory, almost precisely on all fours with the instant problem" (pp. 11 and 12 of appellee's brief). The *Burnham* court emphasized that

the summary proceeding in that case was not an action for conversion of the property in question. The following quotations are instructive:

> "Although the mention in the petition of the highest value of the oil as the measure of the reparation due smacks of damages for conversion, the petition as a whole is evidently a summary one for the restoration to the court's administrator of property wrongfully taken from its custody. The petition makes no allegation as to the title to the oil, but alleges only that it was from an oil lease which was in the custody of the bankruptcy court and which the petitioner was operating under the court's orders. The prayer is for a summary restoration of the value of the oil." (*Id.* at 341.)
>
> "This not being a suit at law for damages for a conversion of property, there was no right to a jury trial." (*Id.* at 342.)
>
> "The two-year statute, Vernon's Texas Civil Statutes, Art. 5526, applying to 'Actions for detaining the personal property of another, and for converting such property to one's own use' and 'Actions for taking or carrying away the goods and chattels of another', does not control, for this is not an 'action'; and is not based on title and does not seek damages, as has been before pointed out." (*Id.* at 43.)
>
> "As tort-feasors all participants would be jointly and severally liable for the whole damages; but this is not a tort suit, it is an effort to trace assets wrongly taken from the custody of the court and compel their return. We believe each participant is

answerable in equity only for the benefit he got." (*Id.* at 344.)

A consideration of these quotations from *Burnham v. Todd* reveals significant differences between that case and the present case, including the following:

1. The present petition is not "a summary one for the restoration to the court's administrator of property wrongfully taken from its custody."

2. The present prayer is not "for a summary restoration of the value of the" property. Furthermore, the trustee's equity in the property apparently had no value inasmuch as the trustee had recommended, and the bankruptcy court had authorized and directed, that the sale be consummated without net benefit to the estate. [R. 9-15, 27-33.]

3. The present case involves "a suit at law for damages," for which there is the "right to a jury trial."

4. The present action does seek damages, and the California statute of limitation applies.

5. The present suit is not "an effort to trace assets wrongly taken from the custody of the court and compel their return."

6. In the *Burnham* case, "each participant (was) answerable in equity only for the benefit he got" from the property. Whereas Johnston and Burnham took the property and sold it for their own benefit, appellant in the present case handled the escrow for the benefit of the parties to the escrow and received nothing from the property.

A consideration of the quotation from *Burnham v. Todd* on pages 11 and 12 of appellee's brief reveals the following additional significant differences between that case and the present case:

1. The present action's purpose is not to require appellant "to substitute" the property "with money"; the trustee sold the property in the first place without intending to get any money for it. Furthermore, the *Burnham* court first pointed out that "if they (Johnston and Burnham) now had it (the property), without question they might be required summarily to turn it over", before concluding, "Since they have done away with it, with equal certainty they may be required to substitute it with money." In the present case, appellant was nothing more than an escrow holder and never had title or possession of the property.

2. Identification and restoration of the property itself is not impossible in the present case, as it was in *Burnham.* Page 12 of appellee's brief bears out what is obvious from paragraph XII of the trustee's application [R. 3, 6], that the properties were owned by the original buyers and had not been foreclosed but were "available to be foreclosed by the institutional lender." The application itself destroys any notion that the buyers were bona fide purchasers, since (1) they were party to the escrow and knew its terms and (2) paragraph XI alleges that they authorized appellant to close the escrow in the allegedly wrongful manner [R. 3, 5.].

Furthermore, even if the property had been obtained by a bona fide purchaser, appellee's brief

incorrectly states California law on the subject of whether the original owner could recover the property. The case cited by appellee (*Phelps v. American Mortgage Company* (1940), 40 Cal. App. 2d 361, 104 P. 2d 880) admits that there is a distinction "between entrusting a depository with a document totally invalid until delivered, and entrusting him with the indicia of ownership to a valid instrument representing a valid existing obligation." Whereas the *Phelps* case dealt with promissory notes that were live, complete, operative instrument(s) representing an existing and binding obligation", the court contrasted that situation to a fact situation like that of the present case: "The . . . basis of the so-called escrow rule . . . is that the documents that were . . . delivered to the escrow holder to be delivered upon performance of certain conditions, were not binding obligations or deeds until delivered by the escrow holder upon performance of the conditions. When the escrow holder delivered them to the third party without performance of the conditions, he was delivering documents that never had represented binding obligations and never became binding, even as to *bona fide* purchasers, because of lack of a proper delivery." (*Id.* at 885.)

The *Phelps* court assumed, without deciding, that this "escrow rule" was in effect in California; other California courts have applied the rule. The California Supreme Court ruled in *Promis v. Duke* (1929), 208 Cal. 420, 281 P. 613, 615, that the transferee M. E. Duke "took nothing under the deed purporting to transfer and convey the same

to her," and, "even if she were to be regarded as a *bona fide* purchaser for value, it would avail her nothing". (See also, *Los Angeles City High School District v. Quinn* (1925), 195 Cal. 377, 234 Pac. 313.) In the more recent case of *Todd v. Vestermark* (1956), 145 Cal. App. 2d 374, 302 P. 2d 347, 349, California law was expressed as follows: "[A] delivery or recordation by or on behalf of the escrow holder prior to full performance of the terms of the escrow is a nullity. No title passes. (Citations)"

In re Mason C. Jones Company (N.D. Ohio E.D. 1953), 109 F. Supp. 843, is also a case in which a party wrongfully taking property from the custody of the bankruptcy court was ordered to return the property or its approximate value. The referee's certificate indicated that the proceeding was a turnover proceeding, and the referee concluded that "[t]he Court has summary jurisdiction to compel turnover of the property which was once in its possession." (*Id.* at 845.) It was therefore consistent with such a proceeding that the petitioner was ordered to produce "the property *or its approximate value,*" but it is surprising that appellee in the present case would emphasize this language since it is not at all like the adjudication which he desires from the bankruptcy court.

Conclusion.

Appellee's brief goes no further, and cites no cases that go further, than to suggest that summary jurisdiction is available to recover property wrongfully taken from the bankruptcy court and, if return of the property is impossible, to require the party who makes such return impossible to restore to the estate the value of the property. And yet, if this is conceded to be the law, these are not the purposes for which the trustee in the present case invoked the referee's jurisdiction.

It is respectfully submitted that the referee's order denying the motion for dismissal, and the district court's order denying the petition for review and dismissal, should be reversed, and that the cause should be remanded with instructions to enter an order dismissing the Application for Order to Show Cause for Damages for Wrongful Closing of Escrow.

MANATT & PHELPS,
MILTON COPELAND,
Attorneys for Appellant.

Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

MILTON COPELAND